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**Introduced by Senator Ortiz**

February 13, 2004

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An act to amend Section 26909 of the Government Code, relating to special districts.

## LEGISLATIVE COUNSEL'S DIGEST

SB 1272, as introduced, Ortiz. Special districts.

Existing law requires the county auditor to either make or contract for an annual audit of the accounts and records of every special purpose district within the county for which an audit is not otherwise provided.

This bill would require these audits to be performed in accordance with General Accounting Office standards for financial and compliance audits and would impose various other requirements on these audits, thus imposing a state-mandated local program. The bill would require the Controller to review the audits under specified procedures.

The California Constitution requires the state to reimburse local agencies and school districts for certain costs mandated by the state. Statutory provisions establish procedures for making that reimbursement.

This bill would provide that no reimbursement is required by this act for a specified reason.

Vote: majority. Appropriation: no. Fiscal committee: yes. State-mandated local program: yes.

*The people of the State of California do enact as follows:*

- 1 SECTION 1. Section 26909 of the Government Code is  
2 amended to read:



1 26909. (a) The county auditor shall either make or contract  
2 with a certified public accountant or public accountant to make an  
3 annual audit of the accounts and records of every special purpose  
4 district within the county for which an audit by a certified public  
5 accountant or public accountant is not otherwise provided. In each  
6 case, the minimum requirements of the audit shall be prescribed  
7 by the Controller and shall conform to generally accepted auditing  
8 standards.

9 (b) Where an audit of a district's accounts and records is made  
10 by a certified public accountant or public accountant, the  
11 minimum requirements of the audit shall be prescribed by the  
12 Controller and shall conform to generally accepted auditing  
13 standards, and a report thereof shall be filed with the Controller  
14 and with the county auditor of the county in which the district is  
15 located. The report shall be filed within 12 months of the end of  
16 the fiscal year or years under examination.

17 (c) Any costs incurred by the county auditor, including  
18 contracts with, or employment of, certified public accountants or  
19 public accountants, in making an audit of every special purpose  
20 district pursuant to this section shall be borne by the district and  
21 shall be a charge against any unencumbered funds of the district  
22 available for the purpose.

23 (d) For joint districts lying within two or more counties, the  
24 above provisions shall apply to the auditor of the county in which  
25 the treasury is located.

26 (e) The county controller, or ex officio county controller, shall  
27 effect this section in those counties having a county controller, or  
28 ex officio county controller.

29 (f) A special district may, by unanimous request of the  
30 governing board of the special district, with unanimous approval  
31 of the board of supervisors, replace the annual audit with a biennial  
32 audit covering a two-year period or, if the district's annual budget  
33 does not exceed an amount specified by the board of supervisors,  
34 an audit covering a five-year period.

35 Notwithstanding the foregoing provisions of this section to the  
36 contrary, districts shall be exempt from the requirement of an  
37 annual audit if the financial statements are audited by the  
38 Controller to satisfy federal audit requirements.

39 (g) A board of supervisors may substitute a financial review in  
40 accordance with definitions promulgated by the United States

1 General Accounting Office for the audit of a special district as  
2 required by this section, provided that all of the following  
3 conditions are met:

4 (1) The board of supervisors is the governing board of the  
5 district.

6 (2) The special districts revenues and expenditures are  
7 transacted through the county's financial systems.

8 (3) The special district's annual revenues do not exceed one  
9 hundred thousand dollars (\$100,000).

10 *(h) It is the intent of the Legislature in amending this section to*  
11 *promote accountability over public revenues by establishing a new*  
12 *program to review and report on financial and compliance audits*  
13 *of special districts. It is further the intent of the Legislature that the*  
14 *Controller shall have the primary responsibility for implementing*  
15 *and overseeing this program.*

16 *(1) Financial and compliance audits shall be performed in*  
17 *accordance with General Accounting Office standards for*  
18 *financial and compliance audits. The audit guide prepared by the*  
19 *Controller shall be used in the performance of these audits. The*  
20 *Controller shall also require that special district auditors on a*  
21 *biennial basis conduct testing of transactions considered high risk*  
22 *for abuse. The additional testing may either be performed during*  
23 *a special district's regular financial statement audit or as a*  
24 *separate audit. Special districts shall provide funding for all costs*  
25 *associated with conducting the audit of high-risk transactions.*  
26 *Every audit report shall specifically and separately address each*  
27 *of the compliance requirements included in the audit guide, stating*  
28 *whether or not the district is in compliance with those*  
29 *requirements. For each compliance requirement included in the*  
30 *audit guide, every audit report shall further state that the*  
31 *suggested audit procedures included in the audit guide for that*  
32 *requirement were followed in the making of the audit, if that is the*  
33 *case, or, if not, what other procedures were followed. If a special*  
34 *district is not in compliance, the audit report shall state all*  
35 *instances of noncompliance. An independent auditor shall not*  
36 *engage in financial or compliance audits unless, within three years*  
37 *of commencing the first of the audits, and every successive three*  
38 *years thereafter, the auditor completes a quality control review in*  
39 *accordance with General Accounting Office standards. This*  
40 *review shall be conducted by the Controller. The time period*

1 *between commencement of the first audit, or completion of a*  
2 *quality control review and completion of a subsequent quality*  
3 *control review, shall be calculated from the first day of the month*  
4 *following commencement of the audit or completion of the quality*  
5 *control review. To determine the practicability and effectiveness of*  
6 *the audits and audit guide, the Controller shall, on an annual*  
7 *basis, review and monitor the audit reports performed by*  
8 *independent auditors. The Controller shall determine whether*  
9 *audit reports are in conformance with reporting provisions of*  
10 *General Accounting Office standards and shall notify each special*  
11 *district and the auditor regarding each determination. The special*  
12 *district contracting for the financial and compliance audit shall*  
13 *include a statement that provides the Controller access to audit*  
14 *working papers.*

15 (2) (A) *The Controller may perform quality control reviews of*  
16 *audit working papers to determine whether audits are performed*  
17 *in conformity with paragraph (1). The Controller shall*  
18 *communicate the results of his or her reviews to the independent*  
19 *auditor, and the special district for which the review was*  
20 *performed, and shall review his or her findings with the*  
21 *independent auditor.*

22 (B) *Prior to the performance of any quality control reviews, the*  
23 *Controller shall develop and publish guidelines and standards for*  
24 *those reviews. Pursuant to the development of those guidelines and*  
25 *standards, the Controller shall provide opportunity for public*  
26 *comment.*

27 (C) (i) *The Controller shall conduct a quality control review of*  
28 *the audit working papers of the independent auditor who*  
29 *performed the audits for a special district if either of the following*  
30 *applies:*

31 (I) *The Controller has reason to believe that public revenues*  
32 *were not appropriately utilized.*

33 (II) *There is reason to believe that a special district report is*  
34 *false, incomplete, or incorrect.*

35 (ii) *If the quality control review of the Controller indicates that*  
36 *the audit was conducted in a manner that may constitute*  
37 *unprofessional conduct as defined pursuant to Section 5100 of the*  
38 *Business and Professions Code, including, but not limited to, gross*  
39 *negligence resulting in a material misstatement in the audit, the*  
40 *Controller shall refer the case to the California Board of*

1 *Accountancy. If the California Board of Accountancy finds that the*  
2 *independent auditor conducted an audit in an unprofessional*  
3 *manner, the independent auditor is prohibited from performing*  
4 *any audit of a special district for a period of three years, in addition*  
5 *to any other penalties that the California Board of Accountancy*  
6 *may impose.*

7 *(D) In any matter that is referred to the California Board of*  
8 *Accountancy under clause (ii), the Controller may suspend the*  
9 *independent auditor from performing any special district audits*  
10 *pending final disposition of the matter by the California Board of*  
11 *Accountancy if the Controller gives the independent auditor notice*  
12 *and an opportunity to respond to that suspension. The independent*  
13 *auditor shall be given credit for any period of suspension if the*  
14 *California Board of Accountancy prohibits the independent*  
15 *auditor from performing audits of the special district under clause*  
16 *(ii). In no event may the Controller suspend an independent*  
17 *auditor under this subdivision for a period of longer than three*  
18 *years.*

19 *(E) The legislative body of a special district may refer an*  
20 *independent auditor of a special district to the California Board*  
21 *of Accountancy for action pursuant to subparagraph (C) if an*  
22 *audit of a special district was conducted in a manner that may*  
23 *constitute unprofessional conduct as defined by Section 5100 of*  
24 *the Business and Professions Code, including, but not limited to,*  
25 *gross negligence resulting in a material misstatement in the audit.*

26 *(3) The Controller shall conduct any additional audits that are*  
27 *necessary to carry out any of his or her statutory duties and*  
28 *responsibilities. Nothing in this section shall be construed to*  
29 *authorize any special district, or any subcontractor or*  
30 *subrecipient, to constrain, in any manner, the Controller from*  
31 *carrying out any additional audits. However, to the extent that the*  
32 *required financial and compliance audits provide the Controller*  
33 *with the information necessary to carry out his or her*  
34 *responsibilities, the Controller shall plan additional audits as*  
35 *appropriate to avoid any unnecessary duplication of audit efforts.*  
36 *In performing these additional audits, the Controller shall, to the*  
37 *extent deemed appropriate under the circumstances, build upon*  
38 *the work performed during the required financial and compliance*  
39 *audit. The Controller shall receive reimbursement from the special*  
40 *districts for the costs of these additional audits.*

1 SEC. 2. No reimbursement is required by this act pursuant to  
2 Section 6 of Article XIII B of the California Constitution because  
3 the only costs that may be incurred by a local agency or school  
4 district will be incurred because this act creates a new crime or  
5 infraction, eliminates a crime or infraction, or changes the penalty  
6 for a crime or infraction, within the meaning of Section 17556 of  
7 the Government Code, or changes the definition of a crime within  
8 the meaning of Section 6 of Article XIII B of the California  
9 Constitution.

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